

ORDER NO. 6032

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Michael Kubayanda, Chairman;
Ashley E. Poling, Vice Chairwoman;
Mark Acton;
Ann C. Fisher; and
Robert G. Taub

Periodic Reporting
(Proposal Three)

Docket No. RM2021-6

ORDER ON ANALYTICAL PRINCIPLES USED IN PERIODIC REPORTING
(PROPOSAL THREE)

(Issued November 4, 2021)

I. INTRODUCTION

On April 8, 2021, the Postal Service filed a petition pursuant to 39 C.F.R. § 3050.11 requesting that the Commission initiate an informal rulemaking proceeding to consider a change to an analytical principle relating to periodic reports.¹ Proposal Three seeks to modify the analytical principle relating to the calculation of the passthroughs for USPS Marketing Mail Carrier Route Flats. Currently, the Postal

¹ Petition of the United States Postal Service for the Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposal Three), April 8, 2021 (Petition). Proposal Three is attached to the Petition.

Service calculates passthroughs for USPS Marketing Mail Carrier Route Flats on 5-Digit pallets separately from other USPS Marketing Mail Carrier Route Flats. Both USPS Marketing Mail Flats and USPS Marketing Mail Flats on 5-Digit pallets consist of destination network distribution center, destination sectional center facility, and destination delivery unit (DDU) rate cells. Petition, Proposal Three at 2. The Postal Service proposes to combine these two rate categories and calculate passthroughs for all USPS Marketing Mail Carrier Route Flats together for pricing and reporting purposes. *Id.*

II. PROCEDURAL HISTORY

On April 13, 2021, the Commission issued a notice initiating this proceeding, soliciting public comment, and appointing a Public Representative.² On April 28, 2021, Chairman's Information Request No. 1 was issued.³ On May 5, 2021, the Postal Service provided its response to CHIR No. 1.⁴

The Commission received comments from the Public Representative on June 1, 2021.⁵ No other party submitted comments.

² Notice of Proposed Rulemaking on Analytical Principles Used in Periodic Reporting (Proposal Three), April 13, 2021 (Order No. 5864).

³ Chairman's Information Request No. 1, April 28, 2021 (CHIR No. 1).

⁴ Responses of the United States Postal Service to Chairman's Information Request No. 1, May 5, 2021.

⁵ Public Representative Comments, June 1, 2021 (PR Comments).

III. BACKGROUND

In 2015, the Postal Service established, and the Commission approved, a new price category for USPS Marketing Mail Carrier Route Flats.⁶ This price category is for pieces on 5-Digit pallets that have been presorted to the Carrier Route level or finer. Pallets prepared in this manner had lower bundle sorting costs because they could be directly cross-docked to the DDUs. Petition, Proposal Three at 2. The new price category was intended to incentivize mailers to prepare more of these kinds of pallets. *Id.* As a result of Order No. 2472 in Docket No. R2015-4, the Postal Service reported workshare discounts for USPS Marketing Mail Carrier Route Flats on 5-Digit pallets separately from other USPS Marketing Mail Carrier Route Flats.

The Postal Service reports on USPS Marketing Mail dropship passthroughs for rate categories in the Annual Compliance Report. For nearly all rate categories, the established methodology for calculating passthrough percentages is to divide the discount per piece by the avoided cost per piece.⁷

In 2017, the Postal Service proposed, and the Commission approved, a new and more accurate way to calculate dropship workshare discounts for USPS Marketing Mail.⁸ There are two groups of rates available to mailers sending USPS Marketing Mail Flats. Petition, Proposal Three at 4. For mailings of pieces that weigh less than the breakpoint weight (either 3.3 ounces or 4 ounces), mailers pay by the piece. *Id.* For mailings of pieces that weigh more than the breakpoint weight, mailers pay a combined rate that includes a price per piece and a price per pound. *Id.* Prior to Docket No. RM2017-11, the percentage passthrough calculation methodology included per-pound mailings in the numerator (the discount calculation) but not in the denominator (the

⁶ Docket No. R2015-4, Order on Revised Price Adjustments for Standard Mail, Periodicals, and Package Services Products and Related Mail Classification Changes, May 7, 2015, at 43-44 (Order No. 2472).

⁷ See Docket No. R2021-2, Library Reference PRC-LR-R2021-2/2, July 19, 2021, Excel file "PRC-CAPCALC-MM-R2021-2.xlsx," tab "USPS MM Flats Prst Prebcd," cells I7:I19.

⁸ Docket No. RM2017-11, Order on Analytical Principles Used in Periodic Reporting (Proposal Seven), November 20, 2017 (Order No. 4227).

avoided cost calculation). *Id.* In Docket No. RM2017-11, the Commission approved a new methodology to calculate workshare discounts that includes all pieces above and below the breakpoint, in both the numerator and the denominator. Docket No. RM2017-11, Order No. 4227 at 8. The Postal Service currently reports pieces and pounds separately for USPS Marketing Mail Carrier Route Flats and USPS Marketing Mail Carrier Route Flats on 5-Digit pallets.

$$\frac{((\text{Pound discount} * \text{Pounds above breakpoint}) + (\text{Piece discount} * \text{Pieces below breakpoint}))}{(\text{Avoided cost per pound} * \text{Pounds above and below breakpoint})}$$

As described in the Postal Service's Petition, the formula used to calculate workshare discounts creates anomalous passthroughs. Petition, Proposal Three at 10. The Postal Service explains that Carrier Route Flats are the only USPS Marketing Mail product for which the density discount is sub-divided based on preparation characteristics rather than density tier (e.g., MADC, ADC, High Density, Saturation), which means rates are based on whether the mail is prepared on "direct" pallets or other containers regardless of density tier. *Id.* When preparation characteristics are correlated with other characteristics, such as weight or entry, anomalous passthrough relationships can result that would not occur if the cost avoidance calculation was based on all pieces within the density tier. *Id.* For example, in FY 2020, the passthrough for Carrier Route Flats on 5-Digit pallets entered at the DDU was 55.9 percent, while the passthrough for all other Carrier Route Flats entered at the DDU was 91.3 percent. *Id.* at 11. Although the underlying unit costs were the same for both, approximately 60 percent of all volume for USPS Marketing Mail Carrier Route Flats on 5-Digit pallets was entered at pound-rated prices (above the breakpoint) while only 40 percent of all Carrier Route basic volume was entered at pound-rated prices (above the breakpoint). *Id.* at 8-9. This difference in the mix of pieces above and below the breakpoint causes large differences in passthroughs for Carrier Route Flats and Carrier Route Flats on 5-Digit

pallets. *Id.* at 8. The Postal Service confirms “...maintaining separate reporting of workshare discounts and percentage passthroughs for dropshipped [USPS] Marketing Mail Carrier Route flats creates the possibility that complying with governing regulations will result in unpredictable, if not irrational or impossible, pricing changes.” *Id.* at 12.

IV. PROPOSAL THREE

The Postal Service proposes to equalize the cost avoidance calculation across USPS Marketing Mail density tiers by calculating and reporting on workshare discounts and percentage passthroughs for all USPS Marketing Mail Carrier Route Flats together. *Id.* at 9, 10. Under Proposal Three, the Postal Service would cease reporting on USPS Marketing Mail Carrier Route Flats on 5-Digit pallets separately from other flats. *Id.* at 9.

V. COMMENTS

The Public Representative agrees with the Postal Service’s assertion that reporting for all dropship USPS Marketing Mail Carrier Route Flats together complies with the Commission’s rules regarding workshare discounts. PR Comments at 2. She maintains that the available data are insufficient to permit reasonable evaluation of USPS Marketing Mail Carrier Route Flats on 5-Digit pallets separately from other USPS Marketing Mail Carrier Route Flats. *Id.* The Public Representative asserts there is scant evidence that USPS Marketing Mail Carrier Route Flats on direct pallets have different avoided costs from other USPS Marketing Mail Carrier Route Flats. *Id.* at 3. Considering the lack of differentiation between products in both avoided costs and discounts, she concludes there is no compelling reason to report on workshare discounts for dropshipping separately. *Id.* at 4. She also asserts that Proposal Three would comply with both the worksharing provisions of the Postal Accountability and Enhancement Act of 2006 and the Commission’s new rules regarding workshare discounts. *Id.* at 2.

VI. COMMISSION ANALYSIS

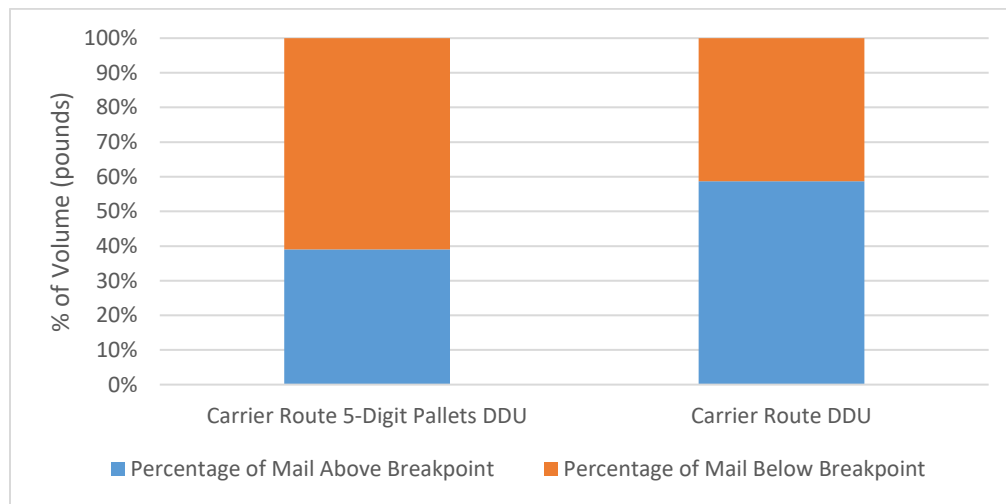
Carrier Route Flats is the only USPS Marketing Mail product for which the density discount is sub-divided based on preparation characteristics rather than density tier. For other products, mail that is more finely presorted by density tier receives a discount. Within Carrier Route, mailings prepared on 5-Digit pallets receive an additional discount even if there is no change in the density tier. The current passthrough calculation inaccurately separates pieces into two distinct groups (when there is little evidence for doing so) and creates a situation wherein it is nearly impossible for all passthroughs to comply with the current worksharing rules.

The Commission agrees with the Public Representative's assertion that "there is no evidence to suggest that the costs avoided by dropshipping[] would depend on whether pieces were prepared on pallets." See PR Comments at 2. The avoided cost estimates are not granular enough to evaluate pieces dropshipped on direct pallets separately.

The passthrough calculation for affected rate categories takes into account the proportion of pieces above and below the breakpoint. As the Postal Service points out, this formula creates passthrough anomalies because the underlying avoided costs are assumed to be the same, yet there are differences in the distribution of pieces above and below the breakpoint for the two rate categories. To elaborate on the Postal Service's point, the numerator of the passthrough formula takes into account the number of pounds above and below the breakpoint to calculate the discount. The denominator of the passthrough formula, however, only takes into account the total number of pounds (with no regard for the percentage above or below the breakpoint) to calculate the avoided cost. This formula leads to a situation where passthroughs for two rate cells can differ even though their underlying costs are the same.

Figure VI-1 illustrates these differences for USPS Marketing Mail Carrier Route Flats dropshipped to the DDU.

Figure VI-1
Percentage of Mail Volume (in Pounds) Above and Below the
Breakpoint for Carrier Route Flats and Carrier Route Flats
on 5-Digit Pallets Dropshipped to the DDU⁹



Source: Library Reference PRC-LR-RM2021-6/1, November 4, 2021, Excel file "PRC-LR1-RM2021-6.xlsx."

Carrier Route Flats dropshipped to the DDU level show the largest difference in pieces above and below the breakpoint. For USPS Marketing Mail Carrier Route Flats dropshipped to the DDU, 59 percent of all pounds are above the breakpoint, while 39 percent of pounds for Carrier Route Flats on 5-Digit pallets are above the breakpoint.¹⁰ This difference in proportions of piece-rated and pound-rated pounds guarantees that at least one passthrough will always be out of compliance. Put differently, under the

⁹ See Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx," tab "Volume Distributions."

¹⁰ Going by piece counts: for Carrier Route Flats on 5-Digit pallets, 9 percent of pieces are above the breakpoint; for Carrier Route Flats on other containers, 26 percent of pieces are above the breakpoint. See Docket No. R2021-2, Library Reference PRC-LR-R2021-2/2, Excel file "PRC-CAPCALC-MM-R2021-2.xlsx," tab "Carrier Route."

current methodology, it is nearly impossible for the Postal Service to set discounts such that all rate categories have passthroughs that fall between 85 percent and 100 percent.

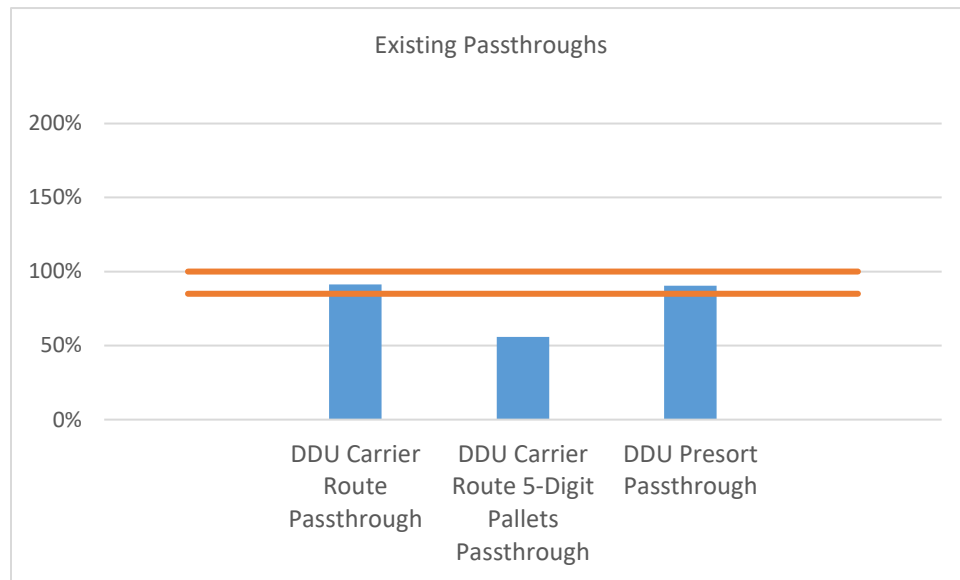
Table VI-1
Calculation Inputs for DDU Rate Cells

Calculation Inputs for Carrier Route Rate Cell	Calculation Input 1	Calculation Input 2
DDU Flats Basic Discount	Basic DDU Dropship	
DDU Flats 5-Digit Discount	5-Digit DDU Dropship	
DDU Flats Presort Discount	Basic DDU Dropship	5-Digit DDU Dropship

Source: Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx."

As shown in Table VI-1, USPS Marketing Mail Carrier Route Flats dropshipped to the DDU have three rate categories associated with them: a dropship discount for Carrier Route Flats (calculated using the discount for Carrier Route Flats); a dropship discount for Carrier Route Flats on 5-Digit pallets (calculated using the discount for Carrier Route Flats on 5-Digit pallets); and a presort discount for Carrier Route Flats on 5-Digit pallets (calculated using both the discount for Carrier Route Flats and the discount for Carrier Route Flats on 5-Digit pallets). Figure VI-2 shows the passthrough for each rate category.

Figure VI-2
Current Passthroughs for Carrier Route Flats Dropshipped to the DDU¹¹

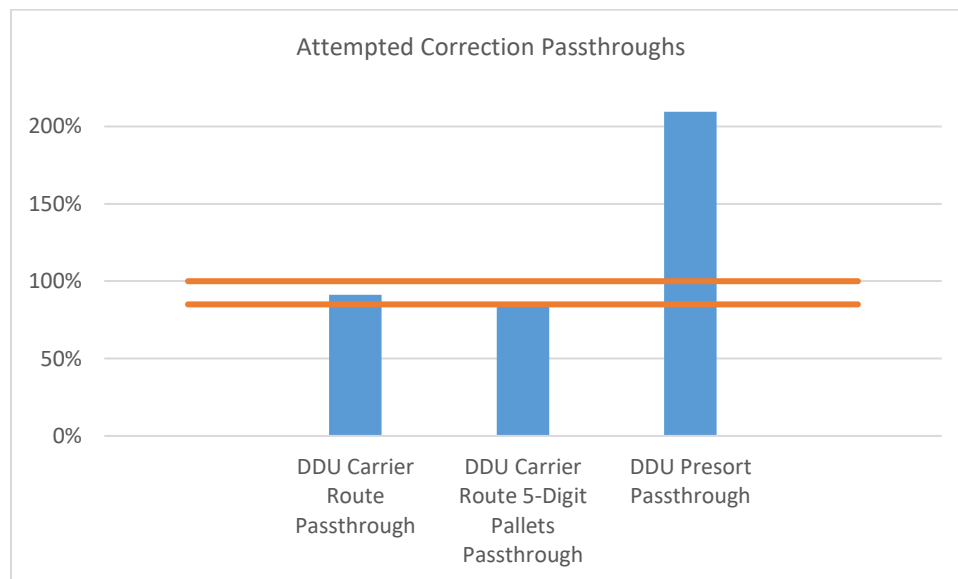


Source: Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx."

¹¹ See Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx," tab "Bar Graph - Current Discounts."

Currently, the dropship passthrough for Carrier Route Flats on 5-Digit pallets is 55 percent. The only way that the Postal Service can raise this passthrough is by increasing the discount for Carrier Route Flats on 5-Digit pallets. However, as demonstrated in Figure VI-3, raising the discount enough to bring the Carrier Route Flats on 5-Digit pallets passthrough up to 85 percent would cause the passthrough for the presort discount to rise all the way to 209 percent. It would be impossible to lower the presort passthrough without pushing the passthrough for USPS Marketing Mail Carrier Route Flats out below 85 percent.

Figure VI-3
DDU Passthroughs Resulting from Bringing 5-Digit Pallets to 85 Percent¹²



Source: Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx."

¹² See Library Reference PRC-LR-RM2021-6/1, Excel file "PRC-LR1-RM2021-6.xlsx," tab "Bar Graph - Current Discounts."

VII. CONCLUSION

Based upon a review of the Postal Service's filings, supporting workpapers, and response to CHIR No. 1, and the Public Representative's comments, the Commission approves Proposal Three. Pursuant to 39 C.F.R. § 3050.42, the Commission finds that the proposed analytical methodology significantly improves the quality, accuracy, and completeness of the Postal Service's workshare discounts. The current methodology of calculating passthroughs for USPS Marketing Mail Carrier Route Flats on 5-Digit pallets separately from other USPS Marketing Mail Carrier Route Flats leads to anomalous results and could precipitate inefficient pricing.

VIII. ORDERING PARAGRAPH

It is ordered:

For purposes of periodic reporting to the Commission, the changes in analytical principles proposed by the Postal Service in Proposal Three are approved.

By the Commission.

Erica A. Barker
Secretary